

Submission to the Treasury Issues Paper on Non-Compete Clauses and other Restraints

31 May 2024

Submission to the Treasury Issues Paper on Non-Compete Clauses and other Restraints	1
About Franchising and the Franchise Council of Australia (FCA).....	1
Overview	2
Comparisons with other markets	2
Restraints derived from Business-Sale Agreements	2
Current Use of Non-Compete Clauses.....	3
Level of Staff Covered by Non-Compete Clauses.....	3
Impact on mobility	4
Areas Where Changes Would Be Welcome	4

About Franchising and the Franchise Council of Australia (FCA)

With more than 94,000 franchise outlets across Australia supporting a workforce of almost 600,000 Australians, the franchise sector is a major employer and economic contributor. Franchising is a sector worth \$174 billion to the Australian economy.

Being part of a franchise network means having access to recruitment and staff development, marketing, HR, technology and IT support, as well as business expertise.

As the peak industry body, the Franchise Council of Australia (FCA) represents franchisors, franchisees and advisors to the franchising community. Together, our focus is on promoting the highest standards of excellence in governance in franchising in Australia. Through its current membership, the FCA has the ability to influence, support and deliver directly to 65,000 franchise outlets.

Our objective as the peak body to this important sector is to drive excellence while also continuing to build connectivity, community and support across all members, whether franchisors or franchisees. This includes an important focus on promoting and supporting our members in regional and rural Australia who are even more relied on at a community level to provide key services.

The FCA welcomes the opportunity to share our views on the current use of non-compete and non-solicitation clauses and thanks Treasury for this opportunity.

Overview

There is a valid use for and reliance on non-disclosure agreements (NDA) and non-solicitation clauses for the protection of confidential information. Government as is the case with business routinely relies on these measures.

The FCA notes that many businesses including our members rely in non-compete and non-solicitation clauses in a reasonable manner to protect legitimate business interests. These are captured under common law as 'legitimate protectable interests'. Importantly, the courts will only uphold these clauses where they 1) only extend to a business' legitimate protectable interests and 2) where they only do so as reasonably necessary to protect those interests.

The FCA supports the position put by ACCI that the codification of non-compete and non-solicitation clauses via the current common law understanding could be a win-win for employees and employers as a result of the greater resulting certainty.

The FCA wholeheartedly endorses the position put by ACCI that all business and organisations have the right to protect their confidential information. It is unreasonable for the Issues Paper to include NDA's or confidentiality agreements in this discussion.

It is also important to reinforce that within the franchise sector, head offices do not have visibility of store contracts. Head office provides standard templates for franchisees to use and adopt as appropriate for their individual, independent businesses.

Comparisons with other markets

Much is made in the paper of the comparative use of non-compete clauses here in comparison to other markets. Non-compete clauses may be used more commonly in Australia compared to other international markets like the United States however Australian employment law provides stronger protections for workers such as redundancy entitlements and unfair dismissal protections. These types of protections are generally not found in U.S. employment systems.

As a result, Australian employers likely rely more heavily on non-compete clauses as part of an employment contract since terminating an Australian worker requires more obligations be met. Due to these differences in baseline employment protections between countries, it is reasonable to expect variations in how and how often non-compete agreements are utilised across international jurisdictions.

Restraints derived from Business-Sale Agreements

The FCA echoes the position of ACCI on the critical need to ensure restraints derived from business-sale agreements which are in the interests of both the vendor (typically a small business) and the purchaser (typically a large business) are not impacted by any reforms.

As part of a sale, there is typically a requirement that the vendor will not compete in the same space for a set time period after the sale. Clearly if this were removed, it would kneecap the value of the asset involved. It's also usual in these circumstances for the vendor's key shareholders/directors and key employees to continue in the business for some set time period to allow the true value of the business to be transferred.

Current Use of Non-Compete Clauses

Non-compete clauses are commonly used within various sectors in Australia to restrict employees and contractors from joining competitors or establishing competing businesses. Their application can be broad, covering geographic regions and specified timeframes.

These clauses are predominantly applied at senior and executive levels where employees have access to sensitive commercial information including sensitive strategic and financial information. At many organisations, non-compete clauses are defined by sector and specific competitors, often including cascading timeframes from 12 months down to three months.

The clauses clearly define restricted competitive businesses, including explicitly naming major competitors. An initial geographic limitation of Australia is set, with flexibility to narrow this if required. A timeframe of 12 months is also written in, but with the option to reduce the period to support reasonable enforceability.

Another member observed that non-compete clauses are often drafted with "waterfall provisions", which make the scope of the restriction as wide as possible initially and then scale it down progressively. For example, a clause may state a wide geographical restriction first, then narrow it down to a specific city, and reduce the time period from years to months.

Non-compete clauses are often drafted with "waterfall provisions", which make the scope of the restriction as wide as possible initially and then scale it down progressively. For example, a clause may state a wide geographical restriction first, then narrow it down to a specific city, and reduce the time period from years to months. Drafting clauses this way allows courts to always read them down to the most reasonable interpretation if the clause is challenged. Waterfall provisions are a way for employers to have a "backstop" while still allowing courts flexibility to assess what is fair and enforceable in a given situation.

It was generally noted that these types of limited provisions are standard across the industry and do not tend to face pushback from employees. While allowing protection of valuable commercial assets, the flexible approach aims to balance this with enabling future job or employer mobility.

In some cases, non-poach clauses are used to prevent poaching staff from other businesses within the same network. However, these clauses are often unenforced due to high worker mobility and the general unenforceability of such provisions. Additionally, some organisations encourage team members to move between locations if necessary due to lifestyle changes.

Various members consulted reinforced the reality that employers in Australia are cautious about using non-compete clauses due to the inevitable legal challenges (all speakers also reinforced the need to protect commercially sensitive IP and information).

Level of Staff Covered by Non-Compete Clauses

The use of non-compete clauses varies significantly across different roles within organisations. While senior executives and key commercial personnel are typically covered by these provisions due to their access to strategic and commercially sensitive information, there is evidence that such clauses are sometimes applied more broadly, even to roles earning lower salaries.

Conversely, some organisations do not include non-compete clauses in their standard employment contracts at the head office level and do not encourage their inclusion in franchisee contracts, except potentially for specific skilled roles.

Impact on mobility

There was a general view that while poaching of staff particularly at a store level is undesirable, team members are encouraged to move between stores if their circumstances necessitate a change.

In those circumstances where migrant workers are engaged, it is obviously a condition of the visa that they work at a particular store. If not, they are in breach of their visa. There is accountability on the business bringing them to Australia to look after them coupled with an accountability by that worker to commit to working for the business for a minimum period of time. This is a win-win situation. What would be helpful here would be a simplification of the process to make the responsibilities for both sides clearer.

Importantly, for those member businesses who support migrant workers, including QSR¹ operations, there is a strong sense that the current approach works well for both the employer and the employee. Removal of the requirement for the migrant worker to stay with the sponsoring business for a set period of time would remove the attraction of sponsorship. Franchise owners in those circumstances simply would not go through the cost and time to bring workers into Australia.

Areas Where Changes Would Be Welcome

The feedback from various members suggests consensus that these clauses should be more targeted and restricted to roles where the protection of genuine business interests is necessary.

Some industry leaders emphasise that retention strategies should focus on creating a positive work environment rather than relying on restrictive clauses. They noted that smart individuals often find ways around such clauses, and it is more effective to invest in strategies that genuinely improve employee satisfaction and loyalty.

Additionally, there are concerns about the enforceability of non-compete clauses, with gardening leave provisions typically serving as the more practical outcome for those roles with access to sensitive information.

Furthermore, there is a need to consider the specific vulnerabilities of migrant workers, who may be particularly restricted by non-compete clauses due to visa conditions that tie them to specific employers. Simplifying industrial relations and providing better support for new migrants are suggested solutions to address these vulnerabilities.

¹ Quick Service Restaurant